

# New Sales Tax Laws Affecting Contractors Beginning July 1, 2004



Supersedes Notice Dated 10/1/2003

With the passage of LB 1017 by the Nebraska Legislature, several changes were made to the laws affecting contractors. These changes become effective on July 1, 2004. These changes include:

- 1 Resale of contractor labor.** All contractors will be permitted to sell their contractor labor tax-free to another contractor;
- 2 Calculating sales tax.** The gross receipts for labor by an Option 2 or Option 3 contractor will be a statutorily determined percentage of the total contract price for building materials and contractor labor, regardless of the actual amounts charged for materials and labor (see "Contractor Labor Percentage"). The total contract price does not include the cost of the raw land, impact fees, title or property insurance, lender fees, closing costs, inspection fees, brokerage fees or taxes levied on the transfer of the property;
- 3 Reporting sales tax.** Contractors must report sales tax on contractor labor when payments are received; and
- 4 75% Major renovation.** Projects involving a major renovation of a commercial or industrial building require prior approval from the department. The application must be signed by a licensed architect or engineer and include payment of a \$500 fee in order for the labor to be tax free.

**Contractor** is any person who repairs property annexed to real estate or who annexes building materials and fixtures to real estate or who arranges for such annexation.

**Labor-only Contracts.** Option 2 and Option 3 contractors who are hired to apply, install, or repair building materials or fixtures owned by another person (labor-only contract) are required to collect sales tax on the contractor labor percentage of the gross receipts.

Option 1 contractors must continue to collect tax on the total amount charged.

## **Collecting and Remitting Tax — Option 2 and Option 3.**

On taxable labor projects, Option 2 and Option 3 contractors must collect and remit sales tax on a percentage of the sales price for building materials and contractor labor (see "Contractor Labor Percentage" discussion). Option 2 and Option 3 contractors are permitted to sell their contractor labor tax-free to another contractor when the sale is supported by a properly completed Nebraska Resale or Exempt Sale Certificate, Form 13.

On exempt labor projects, Option 2 and Option 3 contractors do not collect any sales tax whether billing the project owner or another contractor.

All contractors must report sales tax when payments are received, regardless of when the sale is recorded.

**Contractor Labor Percentage.** Option 2 and Option 3 contractors must use the following percentages when

computing the sales tax due on gross receipts for taxable contractor labor projects:

- Percentage for 7.0% rate is 57.2%;
- Percentage for 6.5% rate is 57.4%;
- Percentage for 6.0% rate is 57.6%; and
- Percentage for 5.5% rate is 57.8%.

These percentages represent 60 percent less an allowance for tax paid on materials at the rate in effect at the location of the job site. For example, sales tax is due on \$57,200 of a \$100,000 taxable labor project ( $\$100,000 \times 57.2\%$ ) located at a site where the rate is 7.0 percent. See the department's Web site for an explanation of the calculation of these percentages.

**Collecting and Remitting Tax — Option 1.** Option 1 contractors are not permitted to use the contractor labor percentage calculation.

On taxable labor projects, Option 1 contractors are required to collect and remit sales tax on the total amount charged for building materials and contractor labor. If the billing is made to another contractor, Option 1 contractors may resell their contractor labor portion of the billing tax-free and only collect tax on the charge for building materials, provided the sale is supported by a properly completed Nebraska Resale or Exempt Sale Certificate, Form 13.

On exempt labor projects, Option 1 contractors are required to collect sales tax on the separately stated materials portion of the invoice whether billing another contractor or billing the project owner.

All contractors must report sales tax when payments are received, regardless of when the sale is recorded.

**Renovation** means the rehabilitation, replacement, or reconfiguration of the walls or fixtures. Renovation does not include merely painting walls or replacing floor coverings, ceilings, siding, windows or a roof.

**Building materials and fixtures** annexed to real estate include, but are not limited to: cabinets, central air conditioners, heat pumps, water heaters, furnaces, insulation, electrical wiring, curtain rods, awnings, concrete, garage door openers, alarm systems, wallpaper, paint, drywall, roofing materials, plumbing, floor coverings, and lumber. Building materials do not include services, such as pest control service, building cleaning services and security services. Such services are subject to tax when purchased by a contractor and cannot be purchased for resale.

All contractors will continue to pay or collect sales tax on their building materials and fixtures based on their contractor option.

**Building** means any freestanding structure annexed to land, enclosed within a roof and exterior walls, regardless of



whether enclosed on all sides. Building includes mobile and modular homes.

**Unit** means a physical portion of a building designated for separate ownership, rental, or occupancy, such as an apartment.

**Structure** means any construction composed of building materials arranged and fitted together in some way. Structure includes items such as bridges, dams, television towers, fences, sidewalks, driveways, decks, billboards, streets, roadways, street lighting, sewers, waterlines, and oil, gas, and water wells.

**Exempt Contractor Labor Charges.** All charges for contractor labor performed in connection with the following projects are exempt from sales and use tax. However, all building materials and fixtures used in such construction projects remain taxable according to the contractor option chosen.

- 1 The first or original construction of a building or other structure;
- 2 The addition of an entire room or floor (story) to any existing building. The addition must actually increase the square footage of the building and the number of rooms or floors in the existing building. The exemption is limited to the charges associated with: the construction of the new room or floor, that part of the existing wall, floor, or ceiling that is altered to accommodate the point of access between the new room or floor and the existing building, and any electrical, plumbing, heating, or cooling system modifications needed to support the new room or floor;
- 3 The completion of an unfinished portion of an existing building or structure;
- 4 The restoration, reconstruction, or replacement of a building or structure damaged or destroyed by fire, flood, tornado, lightning, explosion, ice storm, or natural disaster;
- 5 The construction, repair, or annexation of any structure used for the generation, transmission, or distribution of electricity; or
- 6 **The renovation of an existing building or unit of an existing building when at least 75 percent of the square feet of the building or unit is renovated.** Projects on existing buildings designed for occupancy by one family or a duplex designed for occupancy by two families require the contractor, prior to starting construction, to either notify the department of the nature of the project or obtain approval that the project meets the criteria for a major renovation.

Projects involving the major renovation of commercial or industrial buildings require prior approval from the department in order to exempt the labor from tax. Approval is conditioned upon the filing of an application form and payment of a \$500 application fee. The notification and application forms can be obtained from the department or from our Web site.

The department will send an acknowledgment of notification or an approval of the application, whichever is applicable. The information provided in the notification and application is subject to review and audit by the department.

**100% Major Renovation — Tax on Labor Charges Is Refundable.** When the renovation of an existing building or a unit of an existing building in a single renovation project increases the market value of the building or unit by at least 100 percent, the tax paid on contractor labor charges for such project is refundable to the project owner.

The project owner may obtain a refund by filing a refund claim. The refund claim must include sufficient documentation to substantiate the amount claimed and the change in market value.

This documentation may be disclosed by the department to any tax official in this state.

**Repair and Maintenance Services on Fixtures.** Repair and maintenance performed on buildings, structures, and fixtures, such as air conditioners, furnaces, etc. is taxable. Persons performing such services must collect and remit tax on the taxable labor charges in the same manner as other taxable contractor labor based on their contractor option (see information on "Collecting and Remitting Tax").

The total sales price of a warranty, guarantee, service agreement, or maintenance agreement to cover the costs of replacing, repairing, or maintaining a building, structure, or fixture is taxable. Sales tax must be collected on parts, materials, labor, or any other charge that is not covered under the agreement.

**Tools, Equipment, and Supplies.** All contractors must continue to pay sales or use tax on all purchases of materials, equipment, tools, services and supplies used in providing their contracting, cleaning, maintenance, or repair services. Examples include, but are not limited to, hammers, air compressors, ladders, wrenches, screw drivers, sandpaper, saws, paint thinner, lumber to build forms, office and business equipment, lubricants, solvents, backhoes, cement mixers, scaffolding, pest control services, building cleaning services and security services.

**Sales Tax Permit.** Option 1, Option 2, and Option 3 contractors are retailers and required to obtain a sales tax permit because of their administrative responsibilities for collecting and remitting sales tax. These responsibilities are summarized in our Information Guide titled "Nebraska and Local Sales Tax" on our Web site at: [www.revenue.state.ne.us](http://www.revenue.state.ne.us) or call 1-800-742-7474 (toll free in Nebraska and Iowa) or 1-402-471-5729 if you are calling from outside of Nebraska or Iowa.

**Other Information.** Contractors seeking additional information are encouraged to review the updated information contained in our contractor information guides and the "Questions and Answers" that are posted on our Web site. You may also contact us by calling the telephone numbers listed above.

**Record Keeping.** If your contractor labor charges are exempt from tax, it is necessary that you keep construction contracts, building permits, bid or building specifications, purchase orders, billing invoices, blueprints, drawings, Department of Revenue acknowledgments and approved applications, and any other documentation that contains sufficient information to accurately describe the construction work that was completed.